

## Message Text

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ORIGIN EA-09

INFO OCT-01 ISO-00 FEA-01 ERDA-05 AID-05 CEA-01 CIAE-00

CIEP-01 COME-00 DODE-00 EB-07 FPC-01 H-02 INR-07

INT-05 L-03 NSAE-00 NSC-05 OMB-01 PM-04 USIA-06

SAM-01 OES-06 SP-02 SS-15 STR-04 TRSE-00 ACDA-07 PA-01

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DRAFTED BY EA/IMS:ADORNHEIM:LMG

APPROVED BY EA/EP:GEBER

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FM SECSTATE WASHDC

TO AMEMBASSY JAKARTA

C O N F I D E N T I A L STATE 170577

E.O. 11652:GDS

TAGS: ENRG, ID

SUBJECT:GOI DISCUSSIONS WITH PRODUCTION-SHARING CONTRAC-  
TORS

REF: JAKARTA 8324

1. NATOMAS PRESIDENT COMMONS CALLED UPON GEBER (EA) JULY 8  
WHILE IN WASHINGTON TO KEEP DEPT. ABREAST OF DEVELOPMENTS  
IN ABOVE MATTER.

2. IT WILL BE NATOMAS' TURN SHORTLY TO RESPOND TO GOI'S  
PROPOSALS PRESENTED BY SADLI JUNE 18 (REFTEL). COMMONS IS  
"QUITE CONCERNED," NOT ONLY ABOUT SELF-DEFEATING CHARACTER  
OF GOI'S TERMS BUT ALSO ABOUT "CLOSE TO POISONOUS" ATMO-  
SPHERE IN WHICH NEGOTIATING IS BEING DONE.

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3. ACCORDING COMMONS, NEW ARRANGEMENTS PROPOSED BY GOI

FOR PRODUCTION SHARING CONTRACTORS LEAVE THEM WITH LITTLE, IF ANY, INCENTIVE TO CONTINUE EXPLORING FOR OIL -- WHICH IS OF COURSE FOUNDATION FOR INCOME WHICH GOI IS COUNTING ON OVER NEXT TWO OR THREE DECADES. GOI IS ASKING OIL COMPANIES TO AMORTIZE COSTS OVER PERIODS LONGER THAN

PRODUCTION LIFE OF MOST FIELDS FOUND IN INDONESIA, THUS GREATLY INCREASING RISK THAT PRODUCTION SHARING COMPANIES WILL BE LEFT WITH UNRECOVERED COSTS AFTER ALL PROSPECTS OF GAINING REVENUE FROM THEIR OPERATING AREAS HAVE DISAPPEARED. UNDER SUCH A SETUP, COMMONS BELIEVES THAT OIL COMPANIES WILL SIMPLY PRODUCE WHAT THEY HAVE DEVELOPED AND GET OUT. UNION OIL HAS APPARENTLY ALREADY LET FOUR OF ITS FIVE DRILLING RIGS GO AND IS TRYING TO FARM OUT THE FIFTH.

4. GOI'S NEGOTIATING STANCE ALSO HAS COMMONS WORRIED. WHILE SADLI GIVES LIP SERVICE TO "SPECIAL SITUATION" OF PRODUCTION SHARING COMPANIES, HE QUESTIONS OIL COMPANY DATA ON RESERVES AND FIELD DECLINE RATES, WHICH DATA PERTAMINA ACCEPTS. COMMONS SUSPECTS SADLI IS STRONGLY MOTIVATED BY DESIRE TO SHOW HOW POORLY IBNU HAD DEALT WITH FOREIGN COMPANIES. HE IS CONCERNED ABOUT LOCAL PUBLICITY GIVEN GOI'S GOAL OF A \$2.50 PER BARREL "SHIFT" AND ABOUT SADLI'S COMMENTS THAT FRENCH AND U.S. GOVERNMENTS WERE INTERFERING IN NEGOTIATIONS.

5. IT IS NO SURPRISE, COMMONS SAID, THAT OIL COMPANIES ARE VERY CLOSE TO HAVING NOTHING MORE TO DO WITH INDONESIA IN LIGHT OF ABOVE CONSIDERATIONS AND FACT THAT THERE HAVE BEEN THREE MAJOR CONTRACT CHANGES IN THREE YEARS. EXCEPT PERHAPS FOR LUCKY PETROMER TREND, NONE OF PRODUCING PRODUCTION-SHARERS HAS YET BEEN ABLE TO MAKE A TRUE PROFIT. ALL HAVE BEEN POURING BACK THEIR REVENUES INTO EXPLORATION AND DEVELOPMENT AND HAVE LARGE SUNK COSTS, EXPECTING TO MAKE THEIR PROFITS WHEN ALL POTENTIAL FIELDS HAVE BEEN FOUND AND PLACED ON FULLY OPERATING BASIS.

6. WHILE OTHER PRODUCTION-SHARERS MIGHT NEGOTIATE  
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TOUGHLY WITH GOI, COMMONS SAID NATOMAS IS IN NO POSITION TO DO SO. IT WILL NEVERTHELESS MAKE A COUNTERPROPOSAL WHICH COMMONS ANTICIPATES GOI WILL REJECT. COMMONS THEN STATED THAT IF FINAL GOI OFFER TO NATOMAS LEAVES COMPANY WITH NO REASONABLE EXPECTATION OF RECOVERING ITS HUGE SUNK COSTS (AND PRESUMABLY OF MAKING A REASONABLE (8 PERCENT) RETURN ON INVESTMENT) AND THUS WITH NO INCENTIVE TO CONTINUE EXPLORING, NATOMAS WILL ACCEPT IT

BUT WITH COMMENT THAT ACCEPTANCE WAS INVOLUNTARY. COMMONS PUT THIS THOUGHT ANOTHER WAY: NATOMAS WOULD NOT ACCEPT VOLUNTARILY ANY DEAL WHICH WOULD BE DETRIMENTAL TO INDONESIA IN LONG RUN. COMMONS ALSO REFERRED TO GENERALLY DETRIMENTAL IMPACT OF GOI DEALING WITH OIL COMPANIES ON INVESTMENT CLIMATE.

7. WHILE COMMONS HAS NO DEFINITE PLANS TO GO TO INDONESIA (HE MAY NEED TO PREPARE FOR TESTIMONY BEFORE SENATE FINANCE COMMITTEE WHICH MAY REOPEN PROPOSED AMENDMENT TO TAX REFORM BILL GIVING FIVE YEARS' RELIEF FROM IRS RULING), HE DID ASK FOR EMBASSY SUGGESTIONS ON WHOM ELSE HE MIGHT SEE IN GOI IN EVENT SADLI SHOWS NO REAL APPRECIATION OF NATOMAS PLIGHT. COMMONS SAID SADLI HAD INVITED HIM TO CALL UPON SUHARTO IF NECESSARY, BUT COMMONS DOUBTS EFFICACY OF SUCH A CALL. COMMONS THINKS WIDJOJO OR MALIK MIGHT BE HELPFUL.

8. GEBER INDICATED OUR SYMPATHY WITH PLIGHT OF PRODUCTION SHARING COMPANIES AND SHARED CONCERN ABOUT LONGER-TERM IMPACT ON INDONESIAN OIL EXPLORATION AND ON GENERAL INVESTMENT CLIMATE. DOUBTED, HOWEVER, ABILITY OF USG TO EFFECTIVELY INTERVENE IN INVESTMENT RENEGOTIATIONS. HE OFFERED TO OBTAIN EMBASSY'S VIEWS WHETHER IT MAY BE USEFUL TO PRESENT NATOMAS' CASE EITHER TO MALIK, OR WIDJOJO AND WHETHER EMBASSY COULD ASSIST IN ARRANGING CALL BY COMMONS. EMBASSY'S EARLY RESPONSE IS REQUESTED.

9. EARLIER SAME DAY DEPT OFF TALKED WITH ARCO OFFICIAL. HE REPORTED THAT UNION OIL PEOPLE HAD ALREADY HAD THEIR SESSION WITH GOI AND HAD TOLD INDONESIANS THEIR PROPOSAL WAS UNACCEPTABLE. ARCO'S SESSION SCHEDULED FOR JUNE 9 WITH HARYONO, WHICH MAY BE SIGNIFICANT. ARCO OFFICIAL  
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REITERATED COMMONS CONCERNS NOTED PARA. THREE ABOVE.

10. ON IRS FRONT, COMMONS REPORTED HIS BELIEF THAT IRS HAS NEW GUIDELINES PREPARED BUT IS LOATH TO RELEASE THEM UNTIL SENATE ACTS ON TAX REFORM BILL. HE ADDED THAT HOUSE VERSION OF AMENDMENT BENEFITTING PRODUCTION SHARING COMPANIES WOULD PROVIDE ONLY TWO YEARS RELIEF. KISSINGER

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